BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of	)	
	)	No. 92A-0125-TL
MAZDA MOTORS OF AMERICA	)	
(CENTRAL), INC.	)	

For Appellant: Timothy J. O'Brien
Manager, KPMG Peat Marwick

For Respondent: James H. Peters
Counsel

O P I N I O N

This appeal is made pursuant to section 19045[1/] of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Mazda Motors of America (Central), Inc., against a proposed assessment of additional franchise tax in the amount of $53,171 for the income year ended December 31, 1983.

[1/] Unless otherwise specified, all section references hereinafter in the text of this opinion are to sections of the Revenue and Taxation Code as in effect for the income year in issue.

The sole issue to be determined is whether respondent erred by including receipts from appellant's sales of certain vehicles to a Texas-based distributor in the numerator of the apportionment formula's sales factor.

Appellant is a Delaware corporation with its principal place of business in California. Appellant imports Mazda vehicles and parts from Japan for sale in the United States to its regional distributors, including Mazda Distributors (Gulf), Inc. (MDG), which is located in Texas. MDG in turn sells the vehicles and parts to retail dealers in the Gulf Coast area. The vehicles and parts at issue enter the U.S. through two ports of entry in California. Sometimes, the vehicles are placed in storage facilities maintained by appellant at these two ports awaiting further shipment via common carrier to their ultimate destination. The storage facilities contain body shops and equipment needed to install accessories, such as air conditioning and radios, and to repair the imported vehicles.

According to the Distributor Agreement between appellant and MDG, each vehicle is deemed delivered to MDG at the port of entry at 5:00 p.m. of the first day on which customs clearance is obtained. Parts and accessories installed by appellant on a Mazda vehicle are deemed delivered to MDG at the port of entry at 5:00 p.m. on the date of installation after the marine damage survey of the vehicle is completed and customs clearance has been obtained. Title and risk of loss pass to MDG or its designated financing institution upon delivery at the port of entry. MDG is responsible for all taxes arising after delivery, and payment is made to appellant upon delivery.

According to its Port Processing Agreement with MDG, appellant stores, assembles, installs accessories, repairs, and services vehicles at the port of entry pursuant to MDG's directions. It will insert booklets and documents, like owner's manuals, in the vehicle, and remove stickers and markings. MDG gives appellant custody of the vehicles for this purpose. MDG is required to provide blanket insurance coverage on all vehicles against all losses. Appellant charges MDG for all such services.

Under a "release notice," MDG directs appellant where and to whom to ship the vehicles; no vehicle can be shipped until all work required of appellant is completed. MDG bears all costs of shipment. Under the Mazda Transportation Services Agreement, appellant is required to arrange for the transportation to dealers of vehicles which MDG has sold. For this service, appellant charges MDG $210 per vehicle.

Unlike prior years, some vehicles were serviced by appellant in a Texas facility during the appeal year; all other procedures remained unchanged. The appellant excluded all MDG sales from the numerator of the sales factor on its 1983 California franchise tax return. The respondent initially added back all those sales, but later made adjustments by including in the numerator of the sales factor only those receipts from sales of vehicles which were stored in California while accessories were being installed, repairs were being made, or other services were being performed by appellant, and which appellant subsequently shipped pursuant to MDG's instructions. Receipts from sales of vehicles which were transferred directly to Port Midlothian, Texas, via common carrier after being off-loaded from the

ships in California were excluded. The appellant protested, claiming all its sales to MDG were already taxed under Texas' franchise tax[2/], and submitted a copy of a decision from the Texas Comptroller of Public Accounts to support this assertion. In that case, appellant contended that delivery of those vehicles to MDG occurred in California. Appellant's protest was rejected, and this appeal followed.

The basic measure of the franchise tax imposed on every corporation doing business within California is its net income, from whatever source. (Rev. & Tax. Code, §§ 23151, subd. (a), 24271, 24341; Appeal of Mark IV Metal Products, Inc., Cal. St. Bd. of Equal., Aug. 17, 1982.) However, if a taxpayer has income from sources both within and without California, it is required to allocate and apportion its net income in accordance with the provisions of the Uniform Division of Income for Tax Purposes Act ("UDITPA")[3/], and its California franchise tax liability is measured solely by the net income derived from or attributable to sources within this state. (Rev. & Tax. Code, § 25101.) When a taxpayer conducts a single unitary business both within and without this state, its business income is divided between states by means of an apportionment formula to determine that portion which has its source in California. (Cal. Code Regs., tit. 18, §§ 25101 and 25121.) A taxpayer's business income is apportioned to this state by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three. (Rev. & Tax. Code, § 25128.) The numerators of the respective factors are composed of the taxpayer's property, payroll, and sales in California; the denominators consist of the taxpayer's property, payroll, and sales everywhere. (Rev. & Tax. Code, §§ 25129, 25132, and 25134.)

The rules for determining whether a taxpayer's sales are attributable to California are set forth in section 25135. This section provides, in pertinent part, that sales of tangible personal property are in this state if "[t]he property is delivered or shipped to a purchaser . . . within this state regardless of the f.o.b. point or other conditions of the sale." (Rev. & Tax. Code, § 25135, subd. (a).) "Property is delivered or shipped to a purchaser within this state if the shipment terminates in this state, even though the property is subsequently transferred by the purchaser to another state." (Cal. Code Regs,, tit. 18, § 25135, subd. (a)(3).) This position is supported by the Multistate Tax Commission. (See MTC reg. IV.16(a)(3), [All-St. Tax Guide] St. & Loc. Taxes (RIA) ¶ 662.)

The respondent has defined "delivered" as "the place at which the purchaser takes possession and control of the property" and "shipped" as "the transportation of the property (including delivery) to the purchaser." (FTB LR 348, Jan. 24, 1972.) However, the California Second District Court of Appeal, in interpreting section 25135, held that the phrase "within this state" modifies the word "purchaser", not the words "delivered or shipped." Thus, commercial aircraft delivered in California, but destined for ultimate purchasers outside the state, must be excluded from the numerator of the sales

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[2/] Tex. Tax Code Ann. § 171.001 et seq.

[3/] Rev. & Tax. Code, §§ 25120-25139.

factor. (See McDonnell Douglas Corp. v. Franchise Tax Board, 26 Cal.App.4th 1789 [33 Cal.Rptr.2d 129] (1994).) Appellant contends MDG did not take possession and control of the Mazda vehicles in California and, in any event, respondent's proposed assessment constitutes impermissible multiple taxation under UDITPA and the Multistate Tax Compact.[4/]

We are not persuaded by appellant's claims of non-delivery of the vehicles in question in California, especially in light of the provisions contained in the Distributor, Port Processing, and Transportation Services agreements. The Texas Comptroller's decision is irrelevant as we believe it deals with sales already excluded by respondent. Moreover, appellant's own contractual documents clearly specify that delivery to MDG occurred in California. While MDG may not have taken physical possession of the vehicles in California, it exercised sufficient control over those vehicles to manifest an ownership interest therein. For example, MDG was able to insure the vehicles, direct appellant as to the types of accessories to install, and instruct appellant as to where and to whom to ship them. Also, these activities are indicative of something much more substantive than mere temporary storage in California for purposes of further shipment elsewhere in the stream of interstate commerce.

In addition, we believe the services appellant is obligated to perform under its various agreements with MDG renders McDonnell Douglas inapplicable. While the McDonnell Douglas court made short shrift of Legal Ruling 348, it left unscathed respondent's regulations. We think subdivision (a)(3) of regulation 25135 is of particular relevance, for MDG's activities in California, via its hired agent (appellant), essentially terminated shipment in this state. Such activities are not apparent in McDonnell Douglas, and that court appeared to be concerned with situations involving "dock sales" - i.e., sales where the out-of-state purchaser merely picks up the goods in this state. Respondent has already eliminated such dock sales from the numerator of appellant's sales factor. As mentioned above, subdivision (a)(3) of regulation 25135 has an identical counterpart in regulations written by the Multistate Tax Commission and, thus, should satisfy the McDonnell Douglas court's quest for uniformity. Besides, in light of the level of its activity in California, it cannot be said MDG failed to enjoy any of the benefits and protection provided by this state.

Furthermore, appellant's reliance on the Texas Comptroller's decision is misplaced. We note with particular interest that the Texas Comptroller found, in paragraphs six, seven, and eight of his Findings of Fact, that appellant's contractual documents indicate Texas as the delivery point. As we stated above, the contractual documents submitted herein, and relative to this appeal, point to California as the place of delivery. In addition, the Texas Comptroller makes references to certain paragraphs of documents submitted to him which do not correspond to paragraphs in similarly named documents which were submitted to us. Moreover, the Texas Comptroller's decision deals with vehicles which received customs clearance in Dallas, Texas; the instant appeal concerns vehicles which received customs clearance in California. Thus, we believe the Texas Comptroller and this board are dealing with different transactions. Since the Texas case involved four years (i.e., 1982 through 1985), we

[4/] Rev. & Tax. Code, §§ 38001-38021.

surmise that that tribunal considered sales occurring in 1982, 1984 and 1985, which are not part of this appeal, and the 1983 Texas transactions, which respondent has already excluded from the numerator of appellant's sales factor. Hence, while we are admittedly concerned with the prospect of multiple taxation, we do not believe such taxation to be present in the instant appeal.

For the above reasons, respondent's action in this matter will be sustained.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED, pursuant to section 19047 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Mazda Motors of America (Central), Inc., against a proposed assessment of additional franchise tax in the amount of $53,171 for the income year ended December 31, 1983, be and the same is hereby sustained.

Done at Sacramento, California, this 29th day of November, 1994, by the State Board of Equalization, with Board Members Mr. Sherman, Mr. Fong, Mr. Dronenburg, and Ms. Scott present.

Brad J. Sherman , Chairman

Matthew K. Fong , Member

Ernest J. Dronenburg, Jr. , Member

Windie Scott* , Member

_____ , Member

*For Gray Davis, per Government Code section 7.9.

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